

KEARNS IMPROVEMENT DISTRICT

**FINANCIAL STATEMENTS
with
INDEPENDENT AUDITORS' REPORTS**

DECEMBER 31, 2006

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INDEPENDENT AUDITORS' REPORT

To the Board of Trustees
Kearns Improvement District
Salt Lake City, Utah

We have audited the accompanying basic financial statements of Kearns Improvement District as of and for the year ended December 31, 2006, as listed in the table of contents. These financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these basic financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of Kearns Improvement District as of December 31, 2006, and the results of its operations and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated June 12, 2007, on our consideration of Kearns Improvement District's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

The management's discussion and analysis on pages 4 through 7 is not a required part of the basic financial statements, but is supplementary information required by the Governmental Accounting Standards Board (GASB). We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements of Kearns Improvement District. The schedule of connection fees is presented for purposes of additional analysis and is not a required part of the basic financial statements. The schedule of connection fees has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on it.

June 12, 2007

MANAGEMENT'S DISCUSSION AND ANALYSIS

This section of the Kearns Improvement District's (the District) annual financial report presents our analysis of the District's financial performance during the year ended December 31, 2006. We encourage readers to consider the information presented here in conjunction with the financial statements and accompanying notes to enhance their understanding of the District's financial activities.

Financial Highlights:

- The assets of the District exceeded its liabilities at December 31, 2006 by \$48,161,355. Of this amount, \$13,953,216 may be used to meet the District's ongoing obligations to citizens and creditors.
- The District's total net assets increased by \$2,468,839. This increase is due to operating income from increased rates and capital contributions.
- The District's total debt increased by \$1,132,429. The key factor in this increase is the District's receiving an additional share of Central Valley Water Reclamation Facility's revenue bonds.

Overview of Financial Report:

This annual report consists of two parts: Management's Discussion and Analysis and Financial Statements. The Financial Statements also include notes that explain in more detail some of the information in the financial statements.

Management's Discussion and Analysis (MD&A) serves as an introduction to the basic financial statements and supplementary information. The MD&A represents management's analysis of the District's financial condition and performance.

The financial statements report information about the District using full accrual accounting methods as utilized by similar business activities in the private sector. They include a balance sheet; a statement of revenues, expenses and changes in net assets; a statement of cash flows; and notes to the financial statements. The balance sheet presents the financial position of the District on a full accrual historical cost basis. While the balance sheet provides information about the nature and amount of resources and obligations at year end, the statement of revenues, expenses and changes in net assets presents the results of business activities over the course of the year and information as to how the net assets changed during the year. The statement of cash flows presents changes in cash and cash equivalents, resulting from operating, non-capital and related financing, capital and related financing, and investing activities. In other words, it provides information regarding where the cash came from and how it was used, and the change in cash balance during the reporting period. The notes to the financial statements provide required disclosures and other information that are essential to the full understanding of material data provided in the statements. The notes present information about the District's accounting policies, significant account balances, obligations, commitments, contingencies and subsequent events, if any.

Financial Analysis:

To begin our analysis, a summary of the District's balance sheet is presented in the schedule below.

**Kearns Improvement District
Condensed Balance Sheet**

	<u>2006</u>	<u>2005</u>
Current and Other Assets	\$ 23,545,041	\$ 22,686,502
Capital Assets	<u>45,633,115</u>	<u>42,817,988</u>
Total Assets	<u>\$ 69,178,156</u>	<u>\$ 65,504,490</u>
Current Liabilities	\$ 2,385,759	\$ 2,250,567
Noncurrent Liabilities	<u>18,631,042</u>	<u>17,561,407</u>
Total Liabilities	<u>21,016,801</u>	<u>19,811,974</u>
Net Assets Invested in Capital Assets, Net of Related Debt	32,631,069	29,175,013
Net Assets Restricted	1,577,070	1,638,444
Net Assets Unrestricted	<u>13,953,216</u>	<u>14,879,059</u>
Total Net Assets	<u>48,161,355</u>	<u>45,692,516</u>
Total Liabilities and Net Assets	<u>\$ 69,178,156</u>	<u>\$ 65,504,490</u>

The balance sheet includes all of the District's assets and liabilities, and equity which is categorized as either invested in capital assets, net of related debt; restricted; or unrestricted. Net assets may serve as a useful indicator of a government's financial position. As can be seen from the schedule above, assets exceeded liabilities by \$48,161,355 at the end of the year. The largest portion of the District's net assets, \$32,631,069 (68%), reflects its investment in capital assets, net of related debt (e.g., land, buildings, water and sewer lines, and equipment). The District uses these capital assets in its daily operations; consequently, they are not available for future spending. An additional portion of the District's net assets, \$1,577,070 (3%) represents resources that are subject to external restrictions on how they may be used.

While the balance sheet shows the change in financial position of net assets, the summary of the District's statement of revenues, expenses and changes in net assets, provides information regarding the nature and source of these changes as seen in the following schedule. Net assets increased in 2006 by \$2,468,839.

**Kearns Improvement District
Condensed Statement of Revenues, Expenses, and Changes in Net Assets**

	<u>2006</u>	<u>2005</u>
Operating Revenues	\$ 9,464,446	\$ 8,113,485
Non-operating Revenues	<u>2,765,285</u>	<u>3,029,050</u>
Total Revenues	<u>12,229,731</u>	<u>11,142,535</u>
Depreciation and Amortization Expense	1,730,464	1,411,890
Other Operating Expense	6,994,220	6,561,544
Non-operating Expense	<u>1,677,862</u>	<u>1,517,408</u>
Total Expenses	<u>10,402,546</u>	<u>9,490,842</u>
Income Before Capital Contributions	1,827,185	1,651,693
Capital Contributions	<u>641,654</u>	<u>415,290</u>
Change in Net Assets	2,468,839	2,066,983
Net Assets - Beginning of Year	<u>45,692,516</u>	<u>43,625,533</u>
Net Assets - Ending of Year	<u>\$ 48,161,355</u>	<u>\$ 45,692,516</u>

Net assets increased in 2006 by \$2,468,839 compared to \$2,066,983 in 2005. Key elements of this increase are as follows:

- Operating revenue increased by approximately \$1,351,000 due to lowering usage levels in the first two tiers of the water graduated table, increasing rates in the first three tiers, and increasing fixed monthly charges on water and sewer.

Capital Asset and Debt Administration:

Capital assets. The District's investment in capital assets as of December 31, 2006, amounts to \$45,633,115 (net of accumulated depreciation). This investment in capital assets includes land, buildings, water and sewer systems, and machinery and equipment. The District's investment in capital assets for the current fiscal year increased by 6.6 percent overall.

Major capital asset events during the current fiscal year included the following:

- "Backyard" sewer project construction
- Developer capital contributions
- Purchase of construction equipment for backyard sewer project

Capital Assets Net of Depreciation

	<u>2006</u>	<u>2005</u>
Land	\$ 236,500	\$ 236,500
Buildings and improvements	396,857	397,704
Water system	20,444,339	20,181,000
Sewer transmission and collection lines	23,743,738	21,374,972
Transportation equipment	391,100	431,766
Machinery and equipment	342,636	96,452
Office equipment	<u>77,945</u>	<u>99,594</u>
TOTAL	<u>\$ 45,633,115</u>	<u>\$ 42,817,988</u>

Additional information on the District's capital assets can be found in Note 3.

Long-term debt. At the end of the current fiscal year, the District had total debt of \$19,728,811. The debt represents bonds secured solely by specified revenue sources. The District's debt increased by \$1,132,429 during the current fiscal year due to the District receiving an additional \$2,071,940 in Central Valley Water Reclamation Facility revenue bonds.

The District has no outstanding general obligation debt.

Long-Term Debt

	<u>2006</u>	<u>2005</u>
Revenue bonds, net of deferred amounts on refunding	<u>\$ 19,728,811</u>	<u>\$ 18,596,382</u>

Additional information on the District's long-term debt can be found in Note 5.

Economic Factors and Next Year's Rates:

The District continues to emphasize water conservation while recovering from prior years' drought conditions and being threatened by renewed drought conditions. Amended monthly fixed charges and usage rate increases provided for additional operating revenue. Effective January 1, 2007, the water monthly basic service fee for water meters over ¾" increased by varying amounts, dependent on meter size, and the sewer monthly charge increased by \$2.12 per month. Water usage rates increased by \$0.11, \$0.13, and \$0.17 per thousand gallons, respectively, on the District's first three tiers of its graduated water table.

The District will continue to evaluate the rate structures necessary to assure fiscal responsibility in meeting its operational needs and the requirements for capital improvements according to its water and sewer master plans. A twenty-five year master plan has been created to assist in this process and an independent rate study was performed to accurately identify appropriate increases for 2007 and future years.

Final Comments:

This financial report is designed to provide taxpayers, customers and creditors with a general overview of the District's finances and to demonstrate the District's accountability for the money it receives. If you have questions regarding this report or need additional financial information, contact the Controller of the Kearns Improvement District, 5350 West 5400 South, Kearns, Utah 84118-0608 or by telephone (801) 968-1011.

KEARNS IMPROVEMENT DISTRICT

BALANCE SHEET

DECEMBER 31, 2006

ASSETS

CURRENT ASSETS:

Cash and cash equivalents	\$ 6,637,336
Receivables:	
Property tax	14,097
Water and sewer charges	728,699
Interest receivable	7,084
Inventories	964
Prepaid expenses	34,073
Investments	<u>1,000,219</u>

TOTAL CURRENT ASSETS 8,422,472

NONCURRENT ASSETS:

Restricted cash and cash equivalents	1,577,070
Capital assets (net of accumulated depreciation)	45,633,115
Advances to Central Valley Water Reclamation Facility	74,725
Investment in Central Valley Water Reclamation Facility	13,203,395
Water stock	30,550
Deferred bond issuance costs, net	<u>236,829</u>

TOTAL NONCURRENT ASSETS 60,755,684

TOTAL ASSETS \$ 69,178,156

LIABILITIES AND NET ASSETS

CURRENT LIABILITIES:

Accounts payable	\$ 513,456
Accrued and other liabilities	13,154
Compensated absences	191,185
Customer deposits payable	304,089
Accrued interest on bonds payable	266,106
Revenue bonds payable - current	<u>1,097,769</u>

TOTAL CURRENT LIABILITIES 2,385,759

NONCURRENT LIABILITIES:

Revenue bonds payable (net of unamortized deferred amounts on refunding)	<u>18,631,042</u>
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TOTAL NONCURRENT LIABILITIES 18,631,042

TOTAL LIABILITIES 21,016,801

NET ASSETS:

Invested in capital assets, net of related debt	32,631,069
Restricted for debt service	1,577,070
Unrestricted	<u>13,953,216</u>

TOTAL NET ASSETS 48,161,355

TOTAL LIABILITIES AND NET ASSETS \$ 69,178,156

KEARNS IMPROVEMENT DISTRICT

STATEMENT OF REVENUES, EXPENSES, AND
CHANGES IN NET ASSETS

FOR THE YEAR ENDED DECEMBER 31, 2006

OPERATING REVENUES:

Water sales	\$ 5,898,865
Sewer service charges	3,276,940
Other	<u>288,641</u>

TOTAL OPERATING REVENUES 9,464,446

OPERATING EXPENSES:

Water, sewer, and administrative	6,994,220
Depreciation and amortization	<u>1,730,464</u>

TOTAL OPERATING EXPENSES 8,724,684

OPERATING INCOME 739,762

NON-OPERATING REVENUES (EXPENSES):

Property taxes	1,048,177
Connection fees	1,224,278
Interest income	492,830
Interest expense	(987,958)
Equity in net loss of Central Valley Water Reclamation Facility	<u>(689,904)</u>

TOTAL NON-OPERATING REVENUES 1,087,423

INCOME BEFORE CAPITAL CONTRIBUTIONS 1,827,185

DEVELOPER CONTRIBUTED WATER AND SEWER LINES 641,654

CHANGE IN NET ASSETS 2,468,839

NET ASSETS - BEGINNING OF YEAR 45,692,516

NET ASSETS - END OF YEAR \$ 48,161,355

KEARNS IMPROVEMENT DISTRICT

STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED DECEMBER 31, 2006

CASH FLOWS FROM OPERATING ACTIVITIES:

Receipts from customers and users	\$ 9,275,796
Payments to suppliers	(5,654,068)
Payments to employees	<u>(1,291,821)</u>

NET CASH PROVIDED BY OPERATING ACTIVITIES 2,329,907

CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:

Property taxes collected	<u>1,185,412</u>
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**NET CASH PROVIDED BY NONCAPITAL
FINANCING ACTIVITIES** 1,185,412

**CASH FLOWS FROM CAPITAL AND RELATED FINANCING
ACTIVITIES:**

Connection fees received	1,224,278
Purchases of capital assets	(3,659,429)
Principal paid on capital debt	(1,053,582)
Interest paid on capital debt	<u>(881,594)</u>

**NET CASH (USED IN) CAPITAL AND RELATED
FINANCING ACTIVITIES** (4,370,327)

CASH FLOWS FROM INVESTING ACTIVITIES:

Capital acquisitions in Central Valley Water Reclamation Facility	(110,431)
Interest received	<u>491,391</u>

NET CASH PROVIDED BY INVESTING ACTIVITIES 380,960

NET (DECREASE) IN CASH AND CASH EQUIVALENTS (474,048)

CASH AND CASH EQUIVALENTS - BEGINNING OF YEAR 8,688,454

CASH AND CASH EQUIVALENTS - END OF YEAR \$ 8,214,406

CASH APPEARS ON THE BALANCE SHEET AS FOLLOWS:

Cash and cash equivalents – unrestricted	\$ 6,637,336
Cash and cash equivalents – restricted	<u>1,577,070</u>

\$ 8,214,406

KEARNS IMPROVEMENT DISTRICT

STATEMENT OF CASH FLOWS (CONTINUED)

FOR THE YEAR ENDED DECEMBER 31, 2006

**RECONCILIATION OF OPERATING INCOME TO NET CASH
PROVIDED BY OPERATING ACTIVITIES:**

Operating income	\$ 739,762
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation and amortization	1,730,464
Changes in operating assets and liabilities:	
(Increase) decrease in:	
Receivables	(199,287)
Inventories	955
Prepaid expenses	(8,069)
Increase (decrease) in:	
Accounts payable	114,141
Accrued and other liabilities	(99,522)
Compensated absences	40,826
Customer deposits	<u>10,637</u>

NET CASH PROVIDED BY OPERATING ACTIVITIES

\$ 2,329,907

NON-CASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES:

The District received water and sewer lines from subdividers in the amount of \$641,654 in 2006, which represent the fair value of lines deeded to the District. These additions were accounted for as capital contributions in the statements of revenues, expenses and changes in net assets.

The District recognized its proportionate share of equity in the net loss of Central Valley Water Reclamation Facility in the amount of \$689,904 for the year ended December 31, 2006.

Central Valley Water Reclamation Facility allocated an additional \$7,585,000 in revenue bonds to its members in 2006. The District's share of the additional bonds payable is \$2,071,940 and resulted in an increase in the District's investment in Central Valley Water Reclamation Facility.

KEARNS IMPROVEMENT DISTRICT

NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 2006

1. SUMMARY OF ACCOUNTING POLICIES

A summary of the significant accounting policies consistently applied in the preparation of the accompanying financial statements follows:

A. Reporting Entity

Kearns Improvement District (the District) is a municipal corporation governed by an elected three member board. As required by generally accepted accounting principles, these financial statements present the government and its component units, entities for which the government is considered to be financially accountable. The District is not reported as a component unit of any other entity, and the District has no blended or discretely presented component units.

B. Measurement Focus and Basis of Accounting

The District is an enterprise fund, which is reported using the *economic resources measurement focus* and the *accrual basis of accounting*. An enterprise fund is used to account for operations that are financed and operated in a manner similar to private business enterprises, where the intent of the governing body is that the costs of providing services to the general public on a continuing basis are financed or recovered primarily through user charges. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

The District applies all GASB pronouncements as well as Financial Accounting Standards Board pronouncements issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

Proprietary funds distinguish *operating* revenues and expenses from *nonoperating* items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the District are charges to customers for water and sewer services. Operating expenses include the cost of services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

When both restricted and unrestricted resources are available for use, it is the government's policy to use restricted resources first, then unrestricted resources as they are needed.

C. Deposits and Investments

The District's cash and cash equivalents are considered to be cash on hand, demand deposits and short-term investments with original maturities of three months or less from the date of acquisition.

For purposes of the statement of cash flows, the District considers all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased to be cash equivalents.

Investments are carried at market value or cost where market value is not determinable.

KEARNS IMPROVEMENT DISTRICT

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

1. SUMMARY OF ACCOUNTING POLICIES (CONTINUED)

D. Restricted Cash and Cash Equivalents

Certain resources set aside for bond repayment are classified as restricted on the balance sheet because their use is limited by applicable bond covenants.

E. Inventory

The District's inventory is comprised of water meters, replacement parts and supplies used in the construction and repair of water and sewer lines. The District values its inventory at the lower of cost or market using the first-in, first-out (FIFO) method.

F. Capital Assets

Property and equipment are stated at cost. Normal maintenance and repairs, which neither materially add to the value of the property nor appreciably prolong its life, are charged to expense as incurred. The net book value of property sold or otherwise disposed of is removed from the property and accumulated depreciation accounts and the resulting gain or loss is included in income.

Property, plant, and equipment donated to the District is recorded at the estimated fair value at the date of donation.

Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during the construction phase of fixed assets is reflected in the capitalized value of the asset constructed, net of interest earned on the invested proceeds over the same period. No interest was capitalized during the current fiscal year.

Depreciation of property and equipment is computed using the straight-line method over the following estimated useful lives:

Buildings and Improvements	10-40 years
Water System	25-60 years
Sewer Transmission and Collection Lines	50-60 years
Transportation Equipment	5-7 years
Machinery and Equipment	5-10 years
Office Equipment	5-10 years

G. Joint Venture

The District accounts for its interest in Central Valley Water Reclamation Facility, a joint venture, using the equity method of accounting. See Note 8.

H. Vacation, Sick Leave, and Other Compensated Absences

District employees are entitled to certain compensated absences based on their length of employment.

All vested vacation benefits shall be paid upon termination of employment.

Each December employees are paid for one-fourth of their unused sick leave accumulated that year. The remaining three-fourths are added to unused sick leave accumulated from previous years. Upon retirement, an employee may convert up to 1,000 hours of accumulated sick leave into cash or health insurance coverage. Employees may elect to receive 10% of accumulated sick leave in cash or to apply 25% of accumulated sick leave toward continued health insurance premiums.

KEARNS IMPROVEMENT DISTRICT

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

1. SUMMARY OF ACCOUNTING POLICIES (CONTINUED)

I. Allowance for Doubtful Accounts

The District does not record bad debt expense or an allowance for doubtful accounts on water and sewer fees. Unpaid fees are certified to the county and attached as liens on the related real estate where allowable.

J. Property Tax Revenues

Property taxes are levied on January 1st based on the assessed value of property as listed on the previous May 31st. Assessed values are an approximation of market value. An evaluation of all real property must be made every year by the county assessor. Property taxes are delinquent after November 30. The District's tax rate for 2006 was .000678. The District appropriates the entire amount to operations and maintenance. The statutory maximum set by the state for operations and maintenance is .000800. There is no statutory maximum for the reduction of general obligation bonds.

K. Budgetary Accounting

For management and control purposes, the District adopts and maintains a budget each year. The budget is maintained on a cash basis. Items budgeted, but not expended, are not carried over to succeeding years. Each budget item must be reapproved in each budget year.

2. DEPOSITS AND INVESTMENTS

Deposits and investments for local government are governed by the Utah Money Management Act (*Utah Code Annotated*, Title 51, Chapter 7, "the Act") and by rules of the Utah Money Management Council ("the Council"). Following are discussions of the District's exposure to various risks related to its cash management activities.

A. Deposits

	<u>Bank Balances</u>	<u>Book Balances</u>
Cash on hand	\$ -	\$ 500
Cash on deposit	<u>66,063</u>	<u>62,507</u>
TOTAL	<u>\$ 66,063</u>	<u>\$ 63,007</u>

Custodial Credit Risk: Custodial credit risk is the risk that, in the event of a bank failure, the District's deposits may not be recovered. The District's policy for managing custodial credit risk is to adhere to the Money Management Act. The Act requires all deposits of the District to be in a *qualified depository*, defined as any financial institution whose deposits are insured by an agency of the federal government and which has been certified by the Commissioner of Financial Institutions as meeting the requirements of the Act and adhering to the rules of the Utah Money Management Council. As of December 31, 2006, none of the District's bank balance of \$66,063 was uninsured and uncollateralized.

KEARNS IMPROVEMENT DISTRICT

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

2. DEPOSITS AND INVESTMENTS (CONTINUED)

B. Investments

Credit Risk: Credit risk is the risk that the counterparty to an investment will not fulfill its obligations. The District's policy for limiting the credit risk of investments is to comply with the Money Management Act. The Act requires investments transactions to be conducted only through qualified depositories, certified dealers, or directly with issuers of investment securities. Permitted investments include deposits of qualified depositories; repurchase agreements; commercial paper that is classified as "first tier" by two nationally recognized statistical rating organizations, one of which must be Moody's Investors Services or Standard & Poor's; bankers' acceptances; obligations of the U.S. Treasury and U.S. government sponsored enterprises; bond and notes of political subdivisions of the State of Utah; fixed rate corporate obligations and variable rate securities rated "A" or higher by two nationally recognized statistical rating organizations as defined in the Act.

The District is authorized to invest in the Utah Public Treasurer's Investment fund (PTIF), an external pooled investment fund managed by the Utah State Treasurer and subject to the Act and Council requirements. The PTIF is not registered with the SEC as an investment company, and deposits in the PTIF are not insured or otherwise guaranteed by the State of Utah. The PTIF operates and reports to participants on an amortized cost basis. The income, gains, and losses, net of administration fees, of the PTIF are allocated based upon the participants' average daily balance. The District's investments in Money Market Funds, Grand Cayman, and the PTIF are unrated. The District's investments in U.S. Agencies are rated AAA by Standard & Poor's.

As of December 31, 2006, the District had the following investments and maturities:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Investment Maturities (in Years)</u>			
		<u>Less Than 1</u>	<u>1-5</u>	<u>6-10</u>	<u>More Than 10</u>
Money Market Funds	\$ 8,616	\$ 8,616	\$ -	\$ -	\$ -
Grand Cayman	1,201,243	1,201,243	-	-	-
U.S. Agencies	1,000,219	1,000,219	-	-	-
State of Utah Public Treasurer's Investment Fund	6,941,540	6,941,540	-	-	-
TOTAL	\$ 9,151,618	\$ 9,151,618	\$ -	\$ -	\$ -

Interest Rate Risk: Interest rate risk is the risk that changes in interest rates of debt investments will adversely affect the fair value of an investment. The District manages its exposure to declines in fair value by investing mainly in the PTIF and by adhering to the Money Management Act. The Act requires that the remaining term to maturity of investments may not exceed the period of availability of the funds to be invested. The Act further limited the remaining term to maturity of commercial paper to 270 days or less and fixed rate negotiable deposits and corporate obligations to 365 days or less. Maturities of the District's investments are noted above.

Concentration of Credit Risk: Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. The District's policy to reduce this risk is to adhere to the rules of the Money Management Council. The Council's Rule 17 limits investments in a single issuer of commercial paper and corporate obligations to between five and ten percent depending upon the total dollar amount held in the District's portfolio at the time of purchase.

Custodial Credit Risk: For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the District will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The District does not have a formal policy for custodial credit risk.

KEARNS IMPROVEMENT DISTRICT**NOTES TO FINANCIAL STATEMENTS (CONTINUED)****3. CAPITAL ASSETS**

Capital asset activity for the year ended December 31, 2006 was as follows:

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Capital assets, not being depreciated:				
Land	\$ 236,500	\$ —	\$ —	\$ 236,500
TOTAL CAPITAL ASSETS, NOT BEING DEPRECIATED	<u>236,500</u>	<u>—</u>	<u>—</u>	<u>236,500</u>
Capital assets, being depreciated:				
Buildings and improvements	812,865	22,956	—	835,821
Water system	29,338,248	974,370	—	30,312,618
Sewer transmission and collection lines	26,877,978	2,932,516	—	29,810,494
Transportation equipment	1,341,886	65,093	—	1,406,979
Machinery and equipment	633,470	295,403	—	928,873
Office equipment	<u>392,362</u>	<u>10,745</u>	<u>—</u>	<u>403,107</u>
TOTAL CAPITAL ASSETS BEING DEPRECIATED	<u>59,396,809</u>	<u>4,301,083</u>	<u>—</u>	<u>63,697,892</u>
Less accumulated depreciation for:				
Buildings and improvements	(415,161)	(23,803)	—	(438,964)
Water system	(9,157,248)	(711,031)	—	(9,868,279)
Sewer transmission and collection lines	(5,503,006)	(563,750)	—	(6,066,756)
Transportation equipment	(910,120)	(105,759)	—	(1,015,879)
Machinery and equipment	(537,018)	(49,219)	—	(586,237)
Office equipment	<u>(292,768)</u>	<u>(32,394)</u>	<u>—</u>	<u>(325,162)</u>
TOTAL ACCUMULATED DEPRECIATION	<u>(16,815,321)</u>	<u>(1,485,956)</u>	<u>—</u>	<u>(18,301,277)</u>
TOTAL CAPITAL ASSETS, BEING DEPRECIATED, NET	<u>42,581,488</u>	<u>2,815,127</u>	<u>—</u>	<u>45,396,615</u>
CAPITAL ASSETS, NET	<u>\$ 42,817,988</u>	<u>\$ 2,815,127</u>	<u>\$ —</u>	<u>\$ 45,633,115</u>

4. REVENUE BOND FUNDS

The Board of Trustees for the District has adopted certain resolutions pertaining to the issuance of revenue bonds. These resolutions require certain "funds" to be established to account for the District's receipts, disbursements, and bond payments. Such "funds" are restricted accounts within the District's records and are not separate groups of self balancing accounts. The assets held in these funds are restricted for the purpose stipulated in the resolutions.

Restricted assets at December 31, 2006 represent investments restricted for purposes of the Revenue Bond Funds held in trust of \$1,577,070.

KEARNS IMPROVEMENT DISTRICT**NOTES TO FINANCIAL STATEMENTS (CONTINUED)****5. LONG-TERM DEBT*****Revenue Bonds***

The government issues bonds where the government pledges income derived from the acquired or constructed assets to pay debt service. The original amount of revenue bonds issued in prior years was \$18,115,000. Revenue bonds outstanding at December 31, 2006 were as follows:

<u>Purpose</u>	<u>Interest Rates</u>	<u>Amount</u>
Water system	4.05% - 5.35%	\$ 585,000
Water system	4.50% - 4.95%	3,300,000
Sewer lines, refunding	3.80% - 5.00%	5,420,000
Water system	3.40% - 4.85%	2,445,000
Sewer expansion	4.80% - 6.00%	240,000
Sewer lines, refunding	3.50% - 4.90%	<u>1,170,000</u>
		<u>\$13,160,000</u>

Revenue bond debt service requirements to maturity are as follows:

<u>Year Ending December 31,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total Debt Service</u>
2007	\$ 790,000	\$ 626,005	\$ 1,416,005
2008	825,000	589,321	1,414,321
2009	1,335,000	544,287	1,879,287
2010	1,200,000	480,885	1,680,885
2011	1,255,000	424,449	1,679,449
2012-2016	6,490,000	1,193,360	7,683,360
2017-2021	<u>1,265,000</u>	<u>63,625</u>	<u>1,328,625</u>
TOTALS	<u>\$13,160,000</u>	<u>\$ 3,921,932</u>	<u>\$ 17,081,932</u>

The District's revenue bonds require net revenues of at least 125% of the forthcoming year's debt service requirement. The District met the net revenue requirements for the year ended December 31, 2006.

Central Valley Revenue Bonds

During 2005, Central Valley Water Reclamation Facility issued taxable sewer revenue bonds totaling \$35,000,000 to fund the post 1993 ownership of the treatment facility. The bonds bear interest at 3.00%. The District's share of the bonds is \$8,038,751.

Although the revenue bonds are in the name of Central Valley Water Reclamation Facility, the members are responsible to fund debt service requirements over the life of the bonds. The amount distributed to members in the previous year was \$23,000,000. The remaining bond funds drawn down as of December 31, 2006 (\$7,585,000) were used to fund a Central Valley project and have become the members' obligation. The District's share of the \$23,000,000 bonds distributed was \$4,953,407, and its share of the additional draw down of \$7,585,000 is \$2,071,940.

KEARNS IMPROVEMENT DISTRICT**NOTES TO FINANCIAL STATEMENTS (CONTINUED)****5. LONG-TERM DEBT (CONTINUED)**

Central Valley revenue bond debt service requirements to maturity are as follows:

<u>Year Ending December 31,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total Debt Service</u>
2007	\$ 307,769	\$ 201,784	\$ 509,553
2008	310,066	192,551	502,617
2009	314,660	183,249	497,909
2010	333,034	173,809	506,843
2011	344,518	163,818	508,336
2012-2016	1,860,396	658,477	2,518,873
2017-2021	2,138,307	363,845	2,502,152
2022-2024	<u>1,118,015</u>	<u>57,638</u>	<u>1,175,653</u>
TOTALS	<u>\$ 6,726,765</u>	<u>\$ 1,995,171</u>	<u>\$ 8,721,936</u>

The District had no general obligation bonds outstanding at December 31, 2006.

Advance Refundings

The District issued Sewer Revenue and Refunding Bonds, Series 2001 in August 2001. A portion of the proceeds of the bond issue were placed in an irrevocable trust for the purpose of generating resources for all future debt service payments of \$2,745,000 of the Sewer Revenue Bonds, Series 2000. As a result, the refunded bonds are considered to be defeased and the liability was removed from the balance sheet. The reacquisition price exceeded the net carrying amount of the old debt by \$220,266. This amount is being netted against the new debt and amortized over the remaining life of the refunded debt, which is shorter than the life of the new debt issued. As of December 31, 2006, there was \$2,745,000 outstanding on the defeased Sewer Revenue Bonds, Series 2000.

During 2005, the District placed cash in an irrevocable trust for the purpose of generating resources for all future debt service payments of \$725,000 of the Sewer Revenue Bonds, Series 1996, and all remaining future debt service payments of \$3,960,000 of the Sewer Revenue Bonds, Series 2001. The reacquisition price exceeded the net carrying amount of the old debt by \$90,634. This amount was included in interest expense in the prior year. As of December 31, 2006, there was \$0- and \$3,960,000 outstanding, respectively, on the defeased Sewer Revenue Bonds, Series 1996, and the defeased Sewer Revenue Bonds, Series 2001.

Changes in Long-Term Debt

Long-term debt activity for the year ended December 31, 2006 was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Bonds payable:					
Revenue bonds	\$ 13,915,000	\$ -	\$ (755,000)	\$ 13,160,000	\$ 790,000
Less deferred amounts on refunding	(272,025)	-	114,071	(157,954)	-
CVWRF revenue bonds	<u>4,953,407</u>	<u>2,071,940</u>	<u>(298,582)</u>	<u>6,726,765</u>	<u>307,769</u>
TOTAL BONDS PAYABLE	<u>\$ 18,596,382</u>	<u>\$2,071,940</u>	<u>\$ (939,511)</u>	<u>\$ 19,728,811</u>	<u>\$ 1,097,769</u>

KEARNS IMPROVEMENT DISTRICT

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

5. LONG-TERM DEBT (CONTINUED)

Total interest expense incurred on long-term debt for the year ended December 31, 2006 was \$987,958, of which none was capitalized.

6. PROPERTY TAX REVENUE

The District's total tax rate is .000678. The entire amount is used to meet operating and maintenance expenses. Property tax revenue for the year ended December 31, 2006 was \$1,048,177.

7. EMPLOYEE RETIREMENT PLANS

Plan Description:

Kearns Improvement District contributes to the Local Governmental Contributory Retirement System, Local Governmental Noncontributory Retirement system, and a 401(k) Retirement Plan administered by the Utah Retirement Systems (Systems), a cost sharing multiple employer defined benefit pension plan.

Utah Retirement Systems provide refunds, retirement benefits, annual cost of living adjustments, and death benefits to plan members and beneficiaries in accordance with retirement statutes.

The Systems are established and governed by the respective sections of Chapter 49 of the Utah Code Annotated 1953 as amended. The Utah State Retirement Office Act in Chapter 49 provides for the administration of the Utah Retirement Systems and Plans under the direction of the Utah State Retirement Board (Board) whose members are appointed by the Governor. The Systems issue a publicly available financial report that includes financial statements and required supplementary information for the Local Governmental Contributory Retirement System and the Local Governmental Noncontributory Retirement System. A copy of the report may be obtained by writing to the Utah Retirement Systems, 540 East 200 South, Salt Lake City, UT 84102 or by calling (800) 365-8772.

Funding Policy:

Plan members in the Local Governmental Contributory Retirement System are required to contribute 6% of their annual covered salary (all or part may be paid by the employer for the employee) and Kearns Improvement District was required to contribute 7.08% of their annual covered salary from January through June 2006 and 7.58% from July through December 2006. In the Local Governmental Noncontributory Retirement System, Kearns Improvement District was required to contribute 11.09% of their annual covered salary from January through June 2006 and 11.59% from July through December 2006. The contribution rates are the actuarially determined rates. The contribution requirements of the Systems are authorized by statute and specified by the Board.

The Kearns Improvement District contributions to the Local Governmental Contributory Retirement System for the years ending December 31, 2006, 2005 and 2004 were \$26,202, \$23,624 and \$21,282 respectively, and for the Noncontributory Retirement System the contributions for December 31, 2006, 2005 and 2004 were \$139,146, \$121,645 and \$105,529, respectively. The contributions were equal to the required contributions for each year. Total covered payroll for 2006, 2005, and 2004 was \$1,422,646, \$1,277,500, and \$1,190,670, respectively.

KEARNS IMPROVEMENT DISTRICT

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

7. EMPLOYEE RETIREMENT PLANS (CONTINUED)

Funding Policy (continued):

The District offers its employees additional benefits through a 401(k) Plan. The Plan was adopted prior to the adoption limitations imposed by the 1986 Tax Reduction Act as they relate to Section 401(k) plans. The benefits are not available to employees, or their beneficiaries, until termination, retirement, death, or unforeseeable emergency. These funds are administered by the Utah State Retirement System. The employees have the option to contribute amounts in excess of company contributions, but not exceeding statutory limitations.

The District's contributions to this plan for 2006, 2005 and 2004 were \$45,510, \$44,473 and \$49,092, respectively. Employee contributions to this plan for 2006, 2005 and 2004 amounted to \$37,539, \$28,843, and \$21,582, respectively.

The District also participates in an alternative combined defined contribution and deferred retirement plan under Section 401(k) for certain key employees who elected not to participate in the Utah State Retirement System. Under this plan, the District contributed 13.00% of the employees' salaries and wages during 2005 and 2004. The key employees have the option to contribute amounts in excess of company contributions, but not exceeding statutory limitations. The District's contributions to this plan for 2006, 2005 and 2004 were \$-0-, \$27,454, and \$16,231, respectively.

The District does not maintain a Section 457 deferred compensation plan.

8. CENTRAL VALLEY WATER RECLAMATION FACILITY

During 1981, the District entered into a joint venture with four other special districts and two cities. Central Valley Water Reclamation Facility (Central Valley) was organized to construct and operate a regional sewage treatment facility, for the benefit of the seven members. The seven members and their related ownership interest, as of December 31, 2006 are as follows:

	<u>Original Facility</u>	<u>New Expansion</u>	<u>Enhancements</u>	<u>Digesters</u>	<u>Secondaries</u>
Cottonwood Improvement District	19.569%	7.3215%	18.1191%	8.042%	7.1225%
Salt Lake City Suburban Sanitary District #1	25.622	23.6177	24.7780	20.080	22.6557
Granger-Hunter Improvement District	21.124	25.4755	20.2376	25.050	24.9005
Kearns Improvement District	5.978	24.0002	11.2654	28.435	25.7112
Murray City	8.892	6.8421	8.0168	6.280	6.6882
South Salt Lake City	6.120	2.5074	5.0980	1.378	2.5857
Taylorsville-Bennion Improvement District	<u>12.695</u>	<u>10.2356</u>	<u>12.4851</u>	<u>10.735</u>	<u>10.3362</u>
	<u>100.000%</u>	<u>100.0000%</u>	<u>100.0000%</u>	<u>100.000%</u>	<u>100.0000%</u>

KEARNS IMPROVEMENT DISTRICT

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

8. CENTRAL VALLEY WATER RECLAMATION FACILITY (CONTINUED)

The joint venture is administered by a joint administration board. Each member appoints one member to the board, and voting power is not related to ownership. Therefore, each member is equal to another for voting privileges. The joint venture is responsible for adopting a budget and financing its operations, subject to the approval by each of the seven members.

The District accounts for its investment in Central Valley using the equity method of accounting. Summarized financial information of Central Valley as of December 31, 2006 and for the year then ended is as follows (in thousands):

	<u>2006</u>
Total assets	\$ 139,687
Total net assets	106,890
Revenue	10,366
Change in net assets	2,693
The District's interest in:	
Equity	13,203
Net loss	690

The District has recorded in prior years its previous proportionate share (5.978%) of the government grants received by Central Valley as an addition to the District's investments in Central Valley. All expenses (except depreciation) incurred by Central Valley are billed to its members. Accordingly, the District's equity in net losses of Central Valley annually approximates its share of Central Valley's depreciation expense. Audited statements are available at Central Valley Water Reclamation Facility, 800 West Central Valley Road, Salt Lake City, UT 84119.

The District incurred the following costs from the joint venture for the year ended December 31, 2006:

ADMINISTRATION, OPERATIONS AND MAINTENANCE	<u>\$ 1,067,928</u>
TOTAL EQUITY INVESTMENT IN CENTRAL VALLEY WATER RECLAMATION FACILITY	<u>\$13,203,395</u>

9. COMMITMENTS AND CONTINGENCIES

An agreement has been made with Jordan Valley Water Conservancy District, which provides, in general, that the District will purchase a minimum of 7,000 acre feet of water per year from the Conservancy District. During 2006, the District purchased approximately 7,959 acre feet of water, which cost \$3,081,307.

10. RISK MANAGEMENT

The District is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omission; and natural disasters, for which the District insures with the Local Government Trust Risk Pool.

KEARNS IMPROVEMENT DISTRICT

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

11. SUBSEQUENT EVENTS

Subsequent to December 31, 2006, the District issued \$9,990,000 Water and Sewer Revenue and Refunding Bonds, Series 2007. The bonds bear interest at 3.875% to 5.000% and mature on May 1, 2027. Bond proceeds will be used to finance construction and replacement of certain sewer lines and to refund \$6,330,000 of the District's outstanding water revenue bonds.

Subsequent to December 31, 2006, the District entered into separate development agreements with two developers. Under the terms of the agreements, the developers agree to install certain water and sewer improvements, as identified in the District's capital facilities plan, required to service the proposed developments, and the District agrees to reimburse the developers for the cost of these improvements. The agreements set the maximum reimbursement at approximately \$5,072,000 for water improvements and approximately \$4,661,000 for sewer improvements.

OTHER SUPPLEMENTARY INFORMATION

KEARNS IMPROVEMENT DISTRICT

SCHEDULE OF CONNECTION FEES

FOR THE YEAR ENDED DECEMBER 31, 2006

Kearns Improvement District collects water and sewer connection fees. The following is a summary of the connection fees outstanding by year of collection:

<u>Year Collected</u>	<u>Water</u>	<u>Sewer</u>
2006	\$ —	\$ —
TOTAL	<u>\$ —</u>	<u>\$ —</u>

The following capital projects are planned to use the connection fees shown above:

<u>Planned Capital Project (1)</u>	<u>Projected Cost</u>	<u>Anticipated Start Date (2)</u>	<u>Connection Fee Type</u>
Sewer Main Project 1	\$ 343,302	1/31/2007	Sewer
Sewer Main Project 4	\$ 339,171	6/30/2007	Sewer
Sewer Main Project 8	\$ 197,271	6/30/2007	Sewer
Sewer Main Project 10	\$ 490,468	6/30/2007	Sewer
Water Main Project 6	\$ 1,209,655	6/30/2007	Water
Water Main Project 8	\$ 509,860	6/30/2007	Water

- (1) "Capital Project" numbers are taken from the Capital Facilities Plan.
- (2) Start of actual construction by developer. Reimbursement from connection fees will follow by six to twelve months of completion, and will be incrementally reimbursed over one to three years.



PINNOCK, ROBBINS, POSEY & RICHINS

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INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Board of Trustees
Kearns Improvement District

We have audited the financial statements of Kearns Improvement District as of and for the year ended December 31, 2006, and have issued our report thereon dated June 12, 2007. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Kearns Improvement District's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Kearns Improvement District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider certain deficiencies described in the accompanying management letter to be significant deficiencies in internal control over financial reporting (items 1 through 8).

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider items 6 through 8 to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Kearns Improvement District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended for the information of the Board of Trustees, management, and applicable regulatory agencies, and is not intended to be and should not be used by anyone other than these specified parties.

Samuel, Phillips, Casey & Cochran

June 12, 2007



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INDEPENDENT AUDITORS' REPORT ON STATE LEGAL COMPLIANCE

To the Board of Trustees
Kearns Improvement District

We have audited the financial statements of Kearns Improvement District for the year ended December 31, 2006 and have issued our report thereon dated June 12, 2007. Our audit included testwork on the District's compliance with those general compliance requirements identified in the State of Utah Legal Compliance Audit Guide, including:

Public Debt
Cash Management
Purchasing Requirements
Budgetary Compliance

Truth in Taxation and Property Tax
Limitations
Special Districts
Other General Compliance Issues
Impact Fees and Other Development Fees

The District did not receive any major or nonmajor State grants during the year ended December 31, 2006.

The management of the Kearns Improvement District is responsible for the District's compliance with all compliance requirements identified above. Our responsibility is to express an opinion on compliance with those requirements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether material noncompliance with the requirements referred to above occurred. An audit includes examining, on a test basis, evidence about the District's compliance with those requirements. We believe that our audit provides a reasonable basis for our opinion.

The results of our audit procedures disclosed no instances of noncompliance with the requirements referred to above.

In our opinion, Kearns Improvement District, complied, in all material respects, with the general compliance requirements identified above for the year ended December 31, 2006.

This report is intended for the use of Kearns Improvement District's management, Board of Trustees, and applicable state and federal agencies. However, this report is a matter of public record and its distribution is not limited.

June 12, 2007



PINNOCK, ROBBINS, POSEY & RICHINS

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June 12, 2007

To the Board of Trustees
Kearns Improvement District

As part of our audit of the financial statements of Kearns Improvement District (the District), professional standards require that we communicate, in writing, deficiencies in internal control over financial reporting (internal control) that rise to the level of "significant deficiencies" or "material weaknesses" that we identified during our audit of the financial statements.

As we previously discussed, these deficiencies must be communicated even though management may already know about them and may have made a conscious decision to accept these risks because of cost or other considerations. Also, the independent auditor cannot be used as an internal control to overcome internal control deficiencies. With this in mind we are communicating the following matters.

In planning and performing our audit of the financial statements of the District as of and for the year ended December 31, 2006, in accordance with auditing standards generally accepted in the United States of America, we considered the District's internal control as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, we do not express an opinion on the effectiveness of the District's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control that we consider to be significant deficiencies and other deficiencies that we consider to be material weaknesses.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis.

SIGNIFICANT DEFICIENCIES

A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the following deficiencies to be significant deficiencies in internal control:

1. Accounts Receivable/Allowance for Doubtful Accounts

We noted during our audit a deficiency in the design of controls to identify and allow for bad debts in utility accounts receivable. Past due balances from certain terminated customers were included in accounts receivable at December 31, 2006.

Management's Response

Kearns Improvement District will review old accounts receivable and make an entry for allowance for bad debts based on a percentage of outstanding accounts. We are considering using an outside collection agency for old accounts that we can no longer collect through tax certification procedures.

2. Capital Asset Identification and Classification

We noted during our audit a deficiency in the operation of controls to identify and properly classify capital asset additions.

Management's Response

Some capital equipment was charged initially to the backyard sewer project where it was budgeted. Also capital assets were charged to maintenance expenses that were budgeted under this line item. These can be charged directly to capital and equipment.

3. Accounts Payable

We noted during our audit a deficiency in the operation of controls to identify and record expenses near the end of the year in the proper period.

Management's Response

An attempt was made to properly accrue expenses to the proper period. These will be thoroughly reviewed by the accountant and controller and appropriate adjustments made.

4. Accrued Wages Payable

We noted during our audit a deficiency in the design of controls to ensure the proper recording of accrued wages payable. Accrued wages payable was not calculated or recorded.

Management's Response

Accrued wages will be properly reviewed and journalized at year end from the appropriate payroll journals.

5. Prepaid Expenses

We noted during our audit a deficiency in the design of controls to ensure that prepaid insurance premiums are properly recorded. Prepaid health and workers' compensation insurance premiums were recorded as a negative liability instead of as a prepaid expense.

Management's Response

These items were deliberately left in the accounts from which they are normally charged when paid, but an appropriate entry at year end can be made to charge prepaid expenses.

MATERIAL WEAKNESSES

A material weakness is a significant deficiency, or combination of significant deficiencies, that result in more than a remote likelihood that a material misstatement of the financial statements will not

be prevented or detected by the entity's internal control. We believe that the following deficiencies constitute material weaknesses:

6. Accounting Personnel

The District does not train its accounting personnel sufficiently in financial accounting and reporting to ensure correct accounting for more complex transactions or independently produce financial statements which comply with accounting principles generally accepted in the United States of America (GAAP). The District relies on the financial statement audit procedures to identify certain necessary adjustments, reclassifications, and disclosures to produce GAAP financial statements.

Management's Response

We have relied on auditors to summarize, properly classify, and footnote our financial statements. Our computer software and reports need additional work to become GAAP compliant.

7. Equity Investment in Central Valley Water Reclamation Facility

We noted during our audit a deficiency in the operation of controls to ensure that the District's equity investment in Central Valley Water Reclamation Facility (CVWRF) is properly recorded. A portion of capital contributions made during 2006 were misclassified as expenses; furthermore, the District's share of the net loss of CVWRF for the year ended December 31, 2006 was not recorded in the financial statements. Also, additional CVWRF revenue bonds payable and the corresponding increase in the District's equity investment in CVWRF were not recorded.

Management's Response

As our auditors have also audited Central Valley Water Reclamation Facility, we have waited for them to make year end adjustments and appropriate reclassifications on our books.

8. Advance Refunding of Bonds

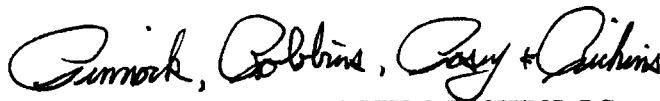
We noted during our audit a deficiency in the operation of controls to properly record interest expense on revenue bonds that have been defeased in full or in part. Interest expense of refunded revenue bonds was recorded in the financial statements, resulting in an overstatement of interest expense.

Management's Response

Classification of payments on refunded and defeased bonds has been somewhat confusing. We can verify the detail of each issue and after discussion with the auditors can correctly classify payments.

Kearns Improvement District's written responses to the significant deficiencies and material weaknesses identified in our audit have not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

This communication is intended solely for the information and use of management, members of the board of trustees of the District, and regulatory agencies, and is not intended to be and should not be used by anyone other than these specified parties.


PINNOCK, ROBBINS, POSEY & RICHINS, PC